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In the Supreme Court of the United States

OCTOBER TERM, 1995

ANNA TWINS SPOTTEDWOLF, ET AL., PETITIONERS

v.

WOODS PETROLEUM CORP., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE DEPARTMENT OF THE INTERIOR IN OPPOSITION

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QUESTION PRESENTED

Whether, in exercising his authority to approve or disapprove proposed agreements to communitize oil and gas leases affecting Indian lands, the Secretary of the Interior may reject a proposed agreement on the ground that it would extend an expiring lease and, thereby, preclude the Indian lessor from obtaining a higher return from a new lease in an improved market.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 4-1 to 4-96) is reported at 47 F.3d 1032. The opinion of the district court (Pet. App. 2-1 to 2-18) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on February 9, 1995. The petition for a writ of certiorari was filed on May 10, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Under the Indian Mineral Leasing Act of 1938, 25 U.S.C. 396a-396g, the Secretary of the Interior is responsible for supervising the leasing of minerals located on lands allotted to Indians. As relevant here, the Act provides that all oil and gas communitization agreements[1] that encompass restricted Indian lands must be approved by the Secretary or his designate. Section 396d of the Act provides in pertinent part:

> In the discretion of the said Secretary, any lease for oil or gas issued under the provisions of sections 396a to 396g of this title shall be made subject to the terms of any reasonable cooperative unit or other plan approved or prescribed by said Secretary prior or subsequent to the issuance of any such lease which involves the development or production of oil or gas from land covered by such lease.

25 U.S.C. 396d. Interior Department regulations promulgated pursuant to the Act, 25 C.F.R. 212.24(b), similarly provide that a communitization agreement that affects Indian mineral rights is not effective without the prior approval of the Secretary. This case concerns the grounds on which the Secretary may disapprove such an agreement.

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[1] Under a "communitization agreement," owners of small tracts of land agree that each owner will benefit from a well drilled anywhere within the communitization unit in proportion to the amount of land that the owner contributed to the unit. See, *e.g.*, *Kenai Oil & Gas, Inc.* v. *Department of Interior*, 671 F.2d 383, 384 (10th Cir. 1982); Cristyn Eddy, *Survey, Land and Natural Resources*, 71 Denv. U. L. Rev. 1017, 1018 n.10 (1994).

1. In February 1977, the Superintendent of the Concho Agency of the Bureau of Indian Affairs (BIA) in the Department of the Interior approved three oil and gas leases between the successors in interest to Walking Woman (deceased), as lessors, and the National Cooperative Refinery Association (National) as lessee. Pet. App. 2-3 to 2-4. Each of the leases had a primary term of five years and provided that it would remain in force "as much longer thereafter as oil and/or gas is produced in paying quantities." *Id.* at 4-6. All three leases contained a "commence drilling clause," which stated that if the lessee commenced drilling of a well within the primary term, the term would be extended, provided that the lessee completed the well with reasonable diligence, and oil or gas was found in paying quantities. *Id.* at 4-6 & n.1. A section of each lease addressed communitization agreements. That section provided that the parties would abide by "any agreement for the cooperative or unit development of the field or area, * * * if and when collectively adopted by a majority operating interest therein and approved by the Secretary of the Interior." *Ibid.* The BIA subsequently approved National's assignment of the leases to respondents. *Id.* at 4-7.

2. The primary terms of the leases were to expire on February 25 and 28, 1982, unless extended by production or communitization. On January 5, 1982, respondent Woods Petroleum Corporation (Woods) commenced drilling of a well on non-Indian lands in the area, and circulated to the other working-interest owners in the area a proposed communitization agreement. In conjunction with the "commence drilling clause" and the ongoing drilling, the communitization clause, if put into effect, would have extended the

terms of the 1977 leases. After obtaining the approval of the majority of working-interest owners, Woods submitted the agreement to the Minerals Management Service of the Department, which recommended approval. Pet. App. 2-5 to 2-6, 4-7.

The proposed agreement was transmitted to the BIA's Anadarko office on February 22, 1982. On the same day, several Indian owners of mineral interests on the leased property delivered objections to the BIA. They maintained that, in light of improved market conditions, it would be in their best interest for the BIA to reject the proposed communitization agreement and allow the leases to expire so that they could negotiate new leases on better terms. Pet. App. 2-6 to 2-7. Nevertheless, on April 12, 1982, the Acting Area Director approved the communitization agreement submitted by Woods. On September 10, 1982, Woods completed its well on non-Indian lands. *Id.* at 2-7.

The Indian mineral owners filed an administrative appeal from the Acting Area Director's decision. During the pendency of the administrative appeal, the Oklahoma Corporation Commission authorized Woods to drill two more wells on non-Indian land within the proposed communitization unit. Royalties from the production of those wells were held in escrow by the Department of the Interior during the appeal. Pet. App. 2-7 to 2-8, 4-9 n.3, 4-10 n.4.

3. While the Department was reviewing the communitization agreement, the court of appeals issued an opinion in a case raising similar issues, *Kenai Oil & Gas, Inc.* v. *Department of Interior*, 671 F.2d 383 (10th Cir. 1982). In *Kenai*, the court upheld the Department's refusal to approve communitization of several Indian oil and gas leases, where the refusal

was based on the fact that "the leases, which had remained unproductive for nearly ten years, could be released for higher royalty payments and bonuses." *Id.* at 387. The *Kenai* court emphasized the Secretary's fiduciary duty to "maximize [Indian] lease revenues," and the absence in the relevant statute and regulations of any provision precluding the Secretary, in disapproving an agreement, from relying on the economic value of re-leasing opportunities. *Id.* at 386. The court, moreover, expressly rejected the lessee's claim that the Secretary was limited to considering matters of conservation and production in deciding whether to approve a communitization agreement. *Id.* at 387.

In response to *Kenai*, the Department issued general guidelines governing the approval of communitization agreements.[2] The guidelines state that the Secretary has discretion to approve or disapprove communitization agreements based on a determination whether approval would be in the best interests of the Indian lessor. In making that determination, the Department is directed to consider: (a) whether the long-term economic effects of the agreement are in the best interest of the Indian lessor; (b) whether, in the judgment of the Interior Department's Minerals Management Service, engineering and technical aspects of the agreement protect the interests of the Indian lessor; and (c) whether the lessee has complied with the terms of the lease. See Pet. App. 4-20.

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[2] Those unpublished guidelines are set out in pertinent part in *Cotton Petroleum Corp.* v. *United States Dep't of Interior*, 870 F.2d 1515, 1517-1518 (10th Cir. 1989).

4. In the instant case, the Deputy Assistant Secretary for Indian Affairs, before whom the Indians' administrative appeal was pending, requested that the Anadarko Area Director provide further information regarding the best interests of the Indian lessors, including prospects for new leases on the land. The Area Director expressed the opinion that approval of the agreement was in the best interests of the lessors. Pet. App. 4-11 to 4-12. The Area Director's analysis was predicated on the assumption that the subject tracts could not profitably be released. See I C.A. App. 117 ("under the present market and economic conditions, the prospect of releasing * * * is not very good"). The Deputy Assistant Secretary circulated that analysis for comment by Woods and the Indian lessors. The Indian lessors' response pointed out that the Area Director's analysis rested on an incorrect factual assumption, because there did in fact exist a potential lessee who was willing to lease the Indian lessors' mineral interests on more lucrative terms. *Id.* at 119.

On May 15, 1986, the Assistant Secretary for Indian Affairs issued his decision, concluding that the Area Director had not acted in the best interests of the Indians in approving communitization. Pet. App. 1-1 to 1-22. Rejecting Woods' claim that disapproval of the agreement would "discourage investors" and "drive away" prospective lessees, the Assistant Secretary noted that a potential lessee (petitioner Tomlinson Properties, Inc.) had offered to pay more than $400,000 in bonuses for new leases on the three tracts. *Id.* at 1-9 to 1-10, 4-12. Observing that *Kenai* held that the Department has a "duty to maximize [Indian] lease revenues," see 671 F.2d at 386, the Assistant Secretary concluded that expiration of the

1977 leases, in light of the definite prospect of new, more lucrative leases, was in the Indians' best interests. Pet. App. 1-10 to 1-11. Accordingly, the Assistant Secretary disapproved Woods' communitization agreement and issued an order declaring that respondents' leases had expired for failure to drill, produce, or communitize during the primary terms. *Id.* at 4-12. Soon thereafter, the Indian lessors and petitioner Tomlinson entered into new leases, which provided for more than $400,000 in bonuses. The Department approved those leases. Tomlinson then submitted a new communitization agreement, retroactive to September 1, 1982, which was approved by BIA's Area Director on September 22, 1986. *Id.* at 2-10 to 2-11, 4-12 to 4-13.

5. On July 28, 1986, Woods filed this action under the Administrative Procedure Act, 5 U.S.C. 701 *et seq.*, seeking to have the Department's decision set aside. On February 22, 1988, the district court upheld the Department's rejection of communitization (Pet. App. 2-1 to 2-18), relying principally on *Kenai*. See *id.* at 2-15.

6. While the appeal of this case was pending, the court of appeals issued opinions in two other cases, taking seemingly conflicting approaches to the question whether the Department may reject communitization on the grounds at issue here. In *Cotton Petroleum Corp.* v. *United States Dep't of Interior*, 870 F.2d 1515 (10th Cir. 1989), the Department had rejected a proposed communitization agreement submitted at the end of a lease's primary term, so that the Indian lessor could take advantage of the improved market for leases in the Anadarko area. The district court found that the Department's action was consistent with *Kenai*, but the court of appeals

reversed, holding that the Secretary acted arbitrarily and capriciously when he "refused to approve an otherwise fair and proper communitization agreement for the *sole purpose* of causing the underlying lease * * * to expire." *Id.* at 1528.

Subsequently, a different panel of the court of appeals held that the Department had breached its fiduciary duty to a Tribe by approving communitization without fully considering the possibility that allowing old leases to lapse might lead to more lucrative new leases. In *Cheyenne-Arapaho Tribes of Oklahoma* v. *United States*, 966 F.2d 583 (10th Cir. 1992), cert. denied, 113 S. Ct. 1642 and 1643 (1993), the court repeated *Kenai*'s admonition that the Secretary has a fiduciary "duty to maximize lease revenues." 966 F.2d at 589 (quoting *Kenai*, 671 F.2d at 386). The Secretary had concluded in *Cheyenne-Arapaho* that disapproval of the proposed agreements would not have been in the Tribe's economic interest because "it was unlikely that new leases would have been negotiated." 966 F.2d at 590. The *Cheyenne-Arapaho* court found, however, that the Secretary "was not free to conclude, without some consideration of the present market conditions, that new leases would be as difficult to negotiate as they would have been in pre-boom times." *Id.* at 591. The court therefore concluded that the "Secretary and his delegates breached their fiduciary responsibilities to the Tribe by failing to consider the market conditions in the Anadarko Area during the 1980's." *Ibid.*

7. On March 7, 1994, a panel of the Tenth Circuit reversed the district court's decision in this case. *Woods Petroleum Corp.* v. *United States Dep't of Interior*, 18 F.3d 854. The panel, relying on *Cotton Petroleum*, held that it was arbitrary and capricious

for the Department to reject communitization for the purpose of allowing the Indian lessors to benefit from the booming market for natural gas in the Anadarko area. The Department, the Indian allottees, and Tomlinson filed petitions for rehearing with suggestions of rehearing en banc, citing the conflict between the panel decision and *Cotton Petroleum*, on the one hand, and *Cheyenne-Arapaho* and *Kenai*, on the other. The full court granted rehearing en banc.

8. The en banc court reached essentially the same result as the panel, with two judges dissenting. Pet. App. 4-1 to 4-96. The majority held that it was an abuse of discretion for the Secretary to reject a communitization agreement "for the sole purpose of causing the expiration of a valid Indian mineral lease and allowing the Indian lessors to enter into a new, more lucrative, lease," where the Secretary then "approves essentially the identical communization [*sic*] agreement, with the new lessee * * * simply substituted for the old lessee." *Id.* at 4-5; see generally *id.* at 4-17 to 4-36.

The court distinguished *Kenai* on the grounds that there, "productive wells had been drilled directly on the Indian land and there was no suggestion that the new lease would be pooled with neighboring tracts"—*i.e.*, the Secretary did not disapprove the proposed communitization agreement with the intention of approving an essentially identical agreement under a new lease. Pet. App. 4-25 to 4-26. The court distinguished *Cheyenne-Arapaho* on the ground that communitization in that case "involved only Indian land, and wells had already been drilled on several of the Indian leases." *Id.* at 4-27. *Cheyenne-Arapaho*, the majority concluded, held simply that the Secretary should have considered the economic value

of new leases, based on changed market conditions. *Ibid.*

Judge Henry, joined by Chief Judge Seymour, dissented, concluding that the Secretary's action in this case was consistent with his fiduciary duty to protect the Indian lessors' economic interests. Pet. App. 4-36 to 4-96. The dissenters asserted that nothing in the relevant statute or regulations prevents the Secretary from considering the manner in which a proposed communitization agreement may affect underlying leases. *Id.* at 4-43 to 4-45. They also believed that, by making the validity of the Secretary's approval or disapproval of a communitization agreement dependent on the existence and disposition of subsequent agreements, the majority's reasoning "deprives [the Secretary] of objective standards that might offer him some guidance as to whether he is making a proper decision at the time he is required to make it." *Id.* at 4-92.

ARGUMENT

We agree with the dissenting judges below (Pet. App. 4-55) that the Tenth Circuit's decisions in *Cotton Petroleum* and the instant case on the one hand, and *Kenai* and *Cheyenne-Arapaho* on the other, present "contrasting principles" regarding the Secretary's obligations under the Indian Mineral Leasing Act. Nonetheless, because the holding in this case is narrow, and because the potential conflict is limited to the Tenth Circuit, further review is not warranted.

Because the Tenth Circuit did not overrule or limit its prior decisions in *Kenai* and *Cheyenne-Arapaho*, the Secretary must continue to consider the economic benefit that Indian lessors would obtain by

disapproval of a proposed communitization agreement and re-leasing under improved market conditions. Pet. App. 4-55. At the same time, however, the Secretary's rejection of a communitization agreement based on that consideration will not be valid under the majority's reasoning if the parties subsequently submit, and the Secretary approves, a similar agreement that covers the Indian lessor and a new lessee. As the dissenting judges noted below (Pet. App. 4-90), by making the validity of the Secretary's action dependent on subsequent events that are frequently beyond his ability to predict, the court's ruling places the Secretary in a "precarious position" where improved market conditions make the prospect of re-leasing attractive.

Although, in our view, the court of appeals' reasoning is flawed, its precise holding in this case is narrow. The court held that

> the Secretary acts arbitrarily and abuses his discretion under § 396d when he (1) rejects a proposed communitization agreement for the sole purpose of causing the expiration of a valid Indian mineral lease and allowing the Indian lessors to enter into a new, more lucrative, lease, and then (2) approves essentially the identical communitization agreement, with the new lessee of the Indian lands simply substituted for the old lessee, and permits the Indian lessors to collect royalties retroactively to the date of first production under the original unit plan.

Pet. App. 4-4 to 4-5. Cf. *id.* at 4-89 (Henry, J., dissenting) (characterizing the majority's holding as "fact-specific"). The decision below therefore appears to leave the Secretary free to disapprove a communi-

tization agreement based on all relevant factors, including the benefit to Indian lessors of a new lease, where he does not subsequently approve a similar communitization agreement under the new lease. *Id.* at 4-25 to 4-26. Contrary to petitioners' contention (Pet. 9), the decision will not in most cases prevent the Secretary from considering, and acting to protect, the economic interests of Indian lessors.

To date, the issue presented in this case has arisen only in the Tenth Circuit. Indeed, three of the four Tenth Circuit cases that have addressed this question (*Cotton Petroleum*, *Cheyenne-Arapaho*, and the instant case) arose from the same natural gas boom market that existed in the Anadarko, Oklahoma, area in the early 1980s. The arguable existence of an intra-circuit conflict regarding the Secretary's obligations under those market conditions does not warrant this Court's review. See, *e.g.*, *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957) ("It is primarily the task of a Court of Appeals to reconcile its internal difficulties.").

Finally, petitioners contend (Pet. 10) that the court of appeals' decision "conflict[s] with applicable decisions of this Court." Petitioners fail, however, to identify any particular decision of this Court with which they believe the instant case is in conflict. The dissenting opinion below, on which petitioners rely (*ibid.*), argues only that the majority erred in applying this Court's administrative law decisions to the facts of this case. See, *e.g.*, Pet. App. 4-76 to 4-77. That argument, though correct in our view, does not warrant this Court's plenary consideration.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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